



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **201314045**
Release Date: 4/5/2013

Date: 1/10/2013

UIL: 501.32-00; 501.33-00; 501.36-01

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear

This is our final determination that you do not qualify for exemption from federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Since you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate state officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your state officials if you have any questions about how this determination may affect your state responsibilities and requirements.

Letter 4038 (CG) (11-2005)
Catalog Number 47632S

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Holly O. Paz
Director, Exempt Organizations
Rulings and Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: October 31, 2012

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

UIL #s

501.32-00

501.33-00

501.36-01

Legend:

B =
D =
U =
V =
W =
X =

Dear

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code ("Code"). Based on the information provided, we have concluded that you do not qualify for exemption under section 501(c)(3) of the Code. The basis for our conclusion is set forth below.

Issue

Do you qualify for exemption under section 501(c)(3) of the Code? No, for the reasons stated below.

Facts

You were established for the purposes of counseling homeowners who are in trouble with their
Letter 4036

mortgage payments, educating non-profit organizations and individuals about the Home Affordable Modification Program and non-governmental housing aid programs, preventing foreclosures, and advocating for consumers on banks' mishandling of loan modifications.

You were incorporated on date D as a nonprofit corporation under state B law. Your Articles of Incorporation state that you are organized exclusively for charitable, religious, educational and scientific purposes including for such purposes the making of distributions to organizations that qualify as exempt organizations under section 501(c)(3) of the Internal Revenue Code, or the corresponding section of any future federal tax code. Your articles also state you are established for the "... purpose of educating, training, motivating and consulting individuals, municipalities and business entities to retain their assets and/or minimize their losses incurred by changes in the economy, their personal economic and financial circumstances and other factors."

Your primary activity is providing one-on-one housing counseling to homeowners in trouble with their mortgages as a U.S. Department of Housing and Urban Development ("HUD") or a certified counseling agency (%). One-on-one housing counseling, mortgage delinquency and default resolution counseling occupies % of your housing counseling activities. The rest of your activities (%) consist of housing and financial seminars, workshops and classes to the public. Your one-on-one housing counseling activities include Home Affordable Modification Program ("HAMP"). HAMP is a HUD program designed to help homeowners who are in trouble with their mortgage payments. You do not have any income or asset limitation for your counseling services. Your clients must have a clear hardship and be eligible for a modification or other forms of mortgage assistance. You define the hardship as follows: reduction of income due to underemployment, reduced pay or hours, decline in business earnings, death, disability or divorce of a borrower or co-borrower; increase in expenses due to monthly payment reset, high medical or health care costs, uninsured losses, increased utilities or property taxes; and excessive monthly debt payments with creditors.

Your housing counseling focuses solely on residential property and is available for various types of mortgage loans up to x dollars including FHA, VA, conventional, fixed, variable, and predatory mortgages. At the initial housing counseling session, you collect the homeowners' most current mortgage statement, financials, and credit report. With the homeowner's authorization, you obtain their mortgage information from lenders. During the session, you explain the aid programs available for homeowners. You did not provide further details regarding how you explain the aid programs. Your initial counseling lasts three hours. You perform a financial analysis that matches the homeowners' needs. At the end of the initial counseling, you provide the homeowners with a monthly financial statement, which shows their income, expenses and debt and an analysis of their mortgage to income ratio and debt to income ratio.

In addition to housing counseling, you offer mortgage delinquency and default resolution counseling services ("resolution services") to homeowners who are either current or delinquent on their mortgage and are financially eligible for a mortgage modification and/or forbearance. For resolution services, you collect general information about the homeowners and the house, a signed and dated limited power of attorney, and other necessary documents. Your home advocacy representatives assist homebuyers in preparing the documentation for submission,

ensure the accuracy and legitimacy of the homeowners' information, prepare the submission package tailored according to the lenders' guideline, follow up on the case, and send additional documents, if necessary. You also negotiate with the lenders directly as an additional service, if needed and requested. The goal of your Resolution Service is for homeowners to have a new payment plan within % of the homeowners' gross income by lowering the interest, principal reduction, and/or forbearance. You did not provide further details how you achieve the lower interest, a principal reduction, and/or forbearance for the homeowners. You conduct a follow-up counseling for the mortgage modification. At follow-up counseling, your counselors update the homeowners on the status of their modifications and advise them about any additional documentation.

A home advocacy representative can handle between 50-70 clients monthly. Your target is to handle 500 clients monthly with a % [front-end debt-to-income] clearance rate. You assign a specific advocate to a homeowner for quick modification, provide homeowners easy access to their data via a secure online portal, and email them biweekly. You provide the homeowners an option that a specific advocate acts as an authorized third party to communicate with lenders directly. You have not submitted an application form to become a HUD or housing counseling agency. We asked for a draft of the form. You did not provide us a draft copy citing you do not have the draft and the filing of the form is dependant on funding.

Your housing and financial seminars, workshops and classes are open to the public. The seminars include an introduction to a mortgage modification and how to apply. The workshops explain how to make a monthly statement, a profit and loss statement, fill in the needed documents for a mortgage modification, and how to present the income sources. You have not conducted housing and financial seminars, workshops and classes. You do not have any curriculum, materials, or any type of funding plan. All your educational activities are dependant on funding.

You are governed by three trustees, U, V, and W. V and W are brother and sister and share the same surname with U. U's and V's duties are "associations with the cities" and recruitment of officers and home advocacy representatives. Both provide 160 hours of services to you per month. W oversees inter non-profit relations, advertising and personal relations, and she provides 80 hours of services to you per month. You indicate a trustee will be compensated at nearly \$100,000. You project that compensation to your governing members will reach x dollars yearly. Your employees will consist of ten home advocacy representatives, five mortgage counselors and five seminar leaders. Home advocacy representatives help your clients apply for a loan modification, update their file, and make sure that the lenders have all the information they need. Mortgage counselors help your clients find the resources and the right program. Seminar leaders are in charge of conducting and organizing the seminars. Two-thirds of your operation will be funded by HUD, certified counseling agencies, and other types of public funding. The rest of your funding will come from receipts from admissions for housing and financial seminars, workshops, classes, educational materials sold, and fundraising events.

Law

Section 501(a) of the Code provides that an organization described in section 501(c)(3) shall be

exempt from taxation.

Section 501(c)(3) of the Code provides that corporations may be exempt from tax if they are organized and operated exclusively for charitable or educational purposes and no part of their net earnings inures to the benefit of any private shareholder or individual.

Section 501(q) of the Code provides that organizations which provide "credit counseling services" as a substantial purpose shall not be exempt from taxation under section 501(a) unless they are described in sections 501(c)(3) or 501(c)(4) and they are organized and operated in accordance with the following requirements:

(1)(A) The organization--

- (i) provides credit counseling services tailored to the specific needs and circumstances of consumers,
- (ii) makes no loans to debtors (other than loans with no fees or interest) and does not negotiate the making of loans on behalf of debtors,
- (iii) provides services for the purpose of improving a consumer's credit record, credit history, or credit rating only to the extent that such services are incidental to providing credit counseling services, and
- (iv) does not charge any separately stated fee for services for the purpose of improving any consumer's credit record, credit history, or credit rating.

(1)(D) At all times the organization has a board of directors or other governing body--

- (i) which is controlled by persons who represent the broad interests of the public, such as public officials acting in their capacities as such, persons having special knowledge or expertise in credit or financial education, and community leaders,
- (ii) not more than 20 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of reasonable directors' fees or the repayment of consumer debt to creditors other than the credit counseling organization or its affiliates), and
- (iii) not more than 49 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of reasonable directors' fees).

Section 501(q)(4)(A) defines, for purposes of section 501(q), the term "credit counseling services" to mean (i) the providing of educational information to the general public on budgeting, personal finance, financial literacy, saving and spending practices, and the sound use of

consumer credit; (ii) the assisting of individuals and families with financial problems by providing them with counseling; or (iii) a combination of the activities described above.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(c)(2) of the regulations provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. Section 1.501(a)-1(c) of the regulations defines the words "private shareholder or individual" in section 501 of the Code to refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an applicant organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable," is used in section 501(c)(3) in its generally accepted legal sense and includes the relief of the poor and distressed or of the underprivileged.

Section 1.501(c)(3)-1(d)(3)(i) of the regulations provides that the term "educational," as used in section 501(c)(3) of the Code, relates to:

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or
- (b) The instruction of the public on subjects useful to the individual and beneficial to the community.

In Rev. Rul. 69-441, 1969-2 C.B. 115, the Service found that a non-profit organization formed to help reduce personal bankruptcy by informing the public on personal money management and aiding low-income individuals and families with financial problems was exempt under section 501(c)(3) of the Code. Its board of directors was comprised of representatives from religious organizations, civic groups, labor unions, business groups, and educational institutions.

The organization provided information to the public on budgeting, buying practices, and the sound use of consumer credit with films, speakers, and publications. It aided low-income individuals and families who have financial problems by providing them with individual counseling and, if necessary, by establishing budget plans. Under the budget plan, the debtor voluntarily made fixed payments to the organization, holding the funds in a trust account and disbursing the funds on a partial payment basis to the creditors. The organization neither

charged fees for counseling services nor prorated their services. The organization did not make loans to debtors or negotiate loans on their behalf. Finally, the organization relied upon contributions, primarily from the creditors participating in the organization's budget plans, for its support. Creditors were not required, though, to make such contributions as a condition of participation.

The Service found that, by aiding low-income individuals and families who have financial problems and by providing, without charge, counseling and a means for the orderly discharge of indebtedness, the organization was relieving the poor and distressed. Moreover, by providing the public with information on budgeting, buying practices, and the sound use of consumer credit, the organization was instructing the public on subjects useful to the individual and beneficial to the community. Thus, the organization was exempt from federal income tax under section 501(c)(3) of the Code.

Revenue Ruling 76-441, 1976-2 C.B. 147, presented two situations concerning school operations. In the first scenario, a nonprofit school succeeded to the assets of a for-profit school. While the former owners were employed in the new school, the board of directors was completely different. The ruling concludes that the transfer did not serve private interests. Part of that conclusion was based on the independence of the board. In the second scenario, the for-profit school converted to a nonprofit school. The former owners became the new school's directors. The former owners/new directors benefited financially from the conversion. The ruling concludes that private interests were served.

Rev. Proc. 86-43, 1986-2 C.B. 729, describes the methodology test the Service uses to determine when the advocacy of a particular viewpoint or position is educational under sections 501(c)(3) of the Code and 1.501(c)(3)-1(d)(3) of the regulations. The revenue procedure states that the focus of section 1.501(c)(3)-1(d)(3) is on the method the organization uses to communicate to others, not the content of its communication. The method of communication is not educational " ... if it fails to provide a development from the relevant facts that would materially aid a listener or reader in a learning process." One factor indicating the method is not educational is as follows: " ... [t]he approach used in the organization's presentations is not aimed at developing an understanding on the part of the intended audience or readership because it does not consider their background or training in the subject matter." The remaining factors relate specifically to advocacy organizations and the "full and fair exposition" part of the regulation.

Rev. Proc. 2012-9, 2012-2 I.R.B. 261, provides that exempt status may be recognized in advance of the organization's operations if its proposed operations are described in sufficient detail to permit a conclusion that it will clearly meet the particular requirements for exemption pursuant to the section of the Code under which exemption is claimed. Section 4.03(2) states that the organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures.

In Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279 (1945), the Supreme Court held that the "presence of a single . . . [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes."

In American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962) cert. denied 372 U.S. 976 (1963), the court considered an organization that provided analyses of securities and industries and of the economic climate in general. It sold subscriptions to various periodicals and services providing advice for purchases of individual securities. The court noted that education is a broad concept, and assumed *arguendo* that the organization had an educational purpose. However, the totality of the organization's activities, which included the sale of many publications as well as the sale of advice for a fee to individuals, was indicative of a business. Therefore, the court held that the organization had a significant non-exempt commercial purpose that was not incidental to the educational purpose, and was not entitled to be regarded as exempt.

In Harding Hospital, Inc. v. United States, 505 F.2d 1068 (6th Cir. 1974), the court held that an organization seeking a ruling as to recognition of its tax-exempt status has the burden of proving that it satisfies the requirements of the particular exemption statute.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the Tax Court found that a corporation formed to provide consulting services did not satisfy the operational test under section 501(c)(3) of the Code because its activities constituted the conduct of a trade or business that is ordinarily carried on by commercial ventures organized for profit. Its primary purpose was not charitable, educational, or scientific, but rather commercial. In addition, the court found that the organization's financing did not resemble that of the typical section 501(c)(3) organizations. It had not solicited, nor had it received, voluntary contributions from the public. Its only source of income was fees from services, and those fees were set high enough to recoup all projected costs and to produce a profit. Moreover, it did not appear that the corporation ever planned to charge a fee less than "cost." Finally, the corporation did not limit its clientele to organizations that were section 501(c)(3) exempt organizations.

In Consumer Credit Counseling Service of Alabama, Inc. v. United States, 44 A.F.T.R. 2d (RIA) 1401 (D.D.C. 1978), the court held that an organization that provided free information on budgeting, buying practices, and the sound use of consumer credit qualified for exemption from income tax because its activities were charitable and educational.

The Consumer Credit Counseling Service of Alabama was an umbrella organization made up of numerous credit counseling service agencies. These agencies provided information to the general public through the use of speakers, films, and publications on the subjects of budgeting, buying practices, and the sound use of consumer credit. They also provided counseling on budgeting and the appropriate use of consumer credit to debt-distressed individuals and families. They did not limit these services to low-income individuals and families, but they did provide such services free of charge. As an adjunct to the counseling function, they offered a debt management plan. Approximately 12 percent of a professional counselor's time was applied to the debt management plan as opposed to education. The agencies charged a

nominal fee of up to \$10 per month for the debt management plan. This fee was waived in instances when payment of the fee would work a financial hardship.

The professional counselors employed by the organizations spent about 88 percent of their time in activities such as information dissemination and counseling assistance rather than those connected with the debt management programs. As such, the community and education counseling assistance programs were the agencies' primary activities. The primary sources of revenue for these organizations were provided by government and private foundation grants, contributions, and assistance from labor agencies and United Way. An incidental amount of their revenue was from service fees. Thus, the court concluded that "each of the plaintiff consumer credit counseling agencies was an organization described in section 501(c)(3) as a charitable and educational organization." See also, Credit Counseling Centers of Oklahoma, Inc. v. United States, 45 A.F.T.R. 2d 80 (D.D.C. 1979), in which the facts were virtually identical and the law was identical to those in Consumer Credit Counseling Service of Alabama, Inc. v. United States, discussed above.

In La Verdad v. Commissioner, 82 T.C. 215 (1984), an organization was formed to provide education and charity, but failed to provide sufficient details regarding its proposed operations. The court held that it failed to prove that it would operate exclusively for exempt purposes under section 501(c)(3) of the Code.

In Easter House v. U.S., 12 Cl. Ct. 476 (1987), aff'd, 846 F. 2d 78 (Fed. Cir.), cert. denied, 488 U.S. 907 (1988), the Claims Court found an organization that operated an adoption agency was not exempt under section 501(c)(3) of the Code because a substantial purpose of the agency was a non-exempt commercial purpose. The court concluded that the organization did not qualify for exemption under section 501(c)(3) because its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court rejected the organization's argument that the adoption services merely complemented the health related services to unwed mothers and their children. Rather, the court found that the health-related services were merely incident to the organization's operation of an adoption service, which, in and of itself, did not serve an exempt purpose. The organization's sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. Accordingly, the court found that the "business purpose, and not the advancement of educational and charitable activities' purpose of plaintiff's adoption service, is its primary goal" and held that the organization was not operated exclusively for purposes described in section 501(c)(3). Easter House, 12 Cl. Ct. at 485-486.

In Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991), the Court of Appeals upheld a Tax Court decision that an organization operating restaurants and health food stores in a manner consistent with the doctrines of the Seventh Day Adventist Church did not qualify for exemption under section 501(c)(3) of the Code because the organization was operated for a substantial non-exempt commercial purpose. The court found that the organization's activities were "presumptively commercial" because the organization was in competition with other restaurants, engaged in marketing, and generally operated in a manner similar to commercial businesses.

In KJ's Fund Raisers, Inc. v. Commissioner, T.C. Memo 1997-424 (1997), aff'd, 82 AFTR 2d 7092 (1998), the Tax Court found that another gaming organization was not exempt. While the organization raised money for charitable purposes, it also operated for the substantial benefit of private interests. The organization's founders, Kristine Hurd and James Gould, were the sole owners of a bar, KJ's Place. The organization, through the owners and employees of KJ's Place, sold lottery tickets exclusively at KJ's Place during regular business hours. While in KJ's Place, the lottery ticket purchasers were sold beverages. The initial directors were Hurd, Gould, and a related individual. The initial board was replaced several times until Hurd and Gould were no longer on the board. At all times Hurd and Gould were the organization's officers. Salaries had been paid to Hurd and Gould and rent had been paid to KJ's Place. The organization maintained that the fact that salaries and rent were no longer paid in this fashion indicated the independence of the board. The Court took another view: "Although those practices ceased and are not in issue here, the current board of directors is composed of at least the majority of the same members who allowed those amounts to be paid." This strongly suggests that Hurd and Gould are free to set policy for their own benefit without objection from the board.

In Airlie Foundation v. Internal Revenue Service, 283 F. Supp. 2d 58 (D.D.C., 2003), the District Court relied on the "commerciality" doctrine in applying the operational test. Because of the commercial manner in which this organization conducted its activities, the court found that it was operated for a non-exempt commercial purpose, rather than for a tax-exempt purpose. As the court stated: "Among the major factors courts have considered in assessing commerciality are competition with for profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include whether the organization uses commercial promotional methods (e.g., advertising) and the extent to which the organization receives charitable donations."

New Dynamics Foundation v. United States, 70 Fed. Cl. 782 (2006), was an action for declaratory judgment that the petitioner brought to challenge the denial of his application for exempt status. The court, in finding that the actual purposes displayed in the administrative record supported the Service's denial, stated "It is well-accepted that, in initial qualification cases such as this, gaps in the administrative record are resolved against the applicant." The court noted that if the petitioner had evidence that contradicted these findings, it should have submitted it as part of the administrative process. The court also highlighted the principle that exemptions from income tax are matters of legislative grace.

Application of Law

Operational Test

To satisfy the 501(c)(3) operational test, an organization must establish that it is operated exclusively for one or more exempt purposes. You failed to establish that you are operated exclusively for one or more exempt purposes. See section 1.501(c)(3)-1(c)(1) of the regulations. Further details for this determination are set forth below.

Your Housing Counseling Activities Are Not Educational

You are distinguishable from the organizations in Consumer Credit Counseling Service of Alabama, above, and Rev. Rul. 69-441 by the methodology you use to conduct your counseling activities because you do not offer housing counseling and resolution services that are structured primarily to improve your clients' understanding of their financial problems or their skills in solving them. It is not an educational activity when you assess and analyze a homeowner's financial situation and prepare loan mitigation paper work, search for the right mitigation channel, and negotiate with lenders for lower mortgage payments, because such work does not provide a development from the relevant facts that would materially aid a listener or reader in a learning process. See Rev. Proc. 86-43, above. During the counseling, you provide information related to housing aid programs and analysis to the homeowners, which may contain some educational methodology; however, you did not provide further explanation or detail how the information is educational. Overall, your housing counseling is not educational. Also, you failed to establish that your interactions with clients provide instruction or training "useful to the individual and beneficial to the community" within the meaning of section 1.501(c)(3)-1(d)(3)(i) of the regulations.

You Are Not Operated Exclusively for Charitable Purposes

More than a substantial amount of your time and resources are devoted to providing housing counseling and resolution services to any individuals who are in a hardship. Your definition of hardship does not include the poor and distressed. Providing the mortgage mitigation service does not provide relief to the poor and distressed within the meaning of section 1.501(c)(3)-1(d)(2) of the regulations or serve any other purpose because these individuals are not necessarily poor and distressed. The individuals who are eligible for a modification or other forms of mortgage assistance include all income level individuals including high-income individuals. Thus, you are unlike the organization described in Rev. Rul. 69-441, above, which aided low-income individuals and families who have financial problems, and relieved the poor and distressed within the meaning of section 1.501(c)(3)-1(d)(2) of the regulations.

You Have a Substantial Non-exempt Purpose

Your application and responses strongly demonstrate that you operate for the substantial commercial purpose of providing housing counseling and resolution services to the public. See Better Business Bureau of Washington D.C., Inc. v. United States, in which the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. Your housing counseling and resolution services are no different from those of a commercial mortgage mitigation business. The fact that your income source is governmental grants would not change your commerciality because the grants are basically the fees that you charge to governments instead of your clients. Furthermore, the fact that you concentrated on housing counseling and resolution services without any educational components indicate commercial motive. In addition, your housing counseling and resolution services directly competes with commercial entities that conduct housing counseling and mortgage mitigation services. The courts found that an organization that conducts a commercial business and competes with commercial companies does not qualify for exemption under 501(c)(3) in Easter House v. U.S. and Living

Faith, Inc. v. Commissioner, regardless of the organizations' doctrines. You therefore do not operate exclusively for exempt purposes. See section 1.501(c)(3)-1(c)(1) of the regulations.

The commerciality doctrine has been debated by numerous courts. The classic cases on the commerciality are found in B.S.W. Group, Inc. v. Commissioner and Airlie Foundation v. Commissioner, above. The courts decisively concluded that running a consulting service and a conference center are not an exempt activity for the reason of commerciality, which is applicable to your housing counseling and resolution services. In addition, the court noted the dependency of the income from the operation, which is also similar to you, since most of your income will come from payments for services. The court in American Institute for Economic Research v. United States, above, applied an even more stringent interpretation. The court held that an educational organization was not entitled to exemption because it conducted the sale of publications as well as the sale of advice for a fee to individuals. You are similar in terms of your selling of resolution services. Accordingly, your commercial activities are evidence of more than an insubstantial non-exempt commercial purpose.

Inurement/Private Benefits

A fundamental requirement for an organization that seeks exemption from federal income taxes is that it benefits the public rather than its creator, shareholders, or persons having a personal or private interest in the activities of the organization. See section 1.501(c)(3)-1(d)(1)(ii) of the regulations. You have not shown that your organizational structure and manner of operation do not result in inurement to your governing members U, V, and W. Your related board of directors, your compensation policies, and your operations do not establish that you are operated for public interests as opposed to private interests. You are similar to the organization in KJ's Fund Raisers, Inc. v. Commissioner in that you do not have checks and balances over your founders' compensation. The court ruled against KJ's Fund Raisers even though it had independent board members. It raised money for charitable purposes but because of the presence of substantial private benefits to the bar owners, the court ruled that KJ's was not exempt. Such private benefits included: the founders were the sole owners of the bar, lottery tickets were sold exclusively at the bar during the regular business hours, beverages were sold to ticket purchasers, and rental payments were made to the bar.

You do not have independent board members, which makes you similar to the second situation in Revenue Ruling 76-441. This ruling confirms the importance of an independent board. The ruling concludes that private interests were served because the former owners became the new school's directors. Your board of directors are related and you have not established how compensation of x dollars to your officers is reasonable. Therefore, you have not establish that the private interests of U, V, and W will not result in inurement.

Section 501(q) of the Code

An organization that provides educational information on financial topics or financial counseling to homeowners who are at risk of foreclosure is providing "credit counseling services" within the meaning of section 501(q)(4)(A) of the Code. Thus to be exempt from taxation you must, in

addition to complying with the requirements of section 501(c)(3), comply with the provisions of section 501(q).

All of your governing members are compensated for the work they provide for you. Therefore, your governing body does not comply with section 501(q)(1)(D)(ii) that requires that at all times the organization must have a board of directors or other governing body not more than 20 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities.

You also do not meet the requirements under section 501(q)(1)(A)(i) of the Code. The Code requires a credit counseling organization to provide credit counseling services tailored to the specific needs and circumstances of consumers. Your service, however, focuses on the mortgage mitigation service. In fact, all you provide is the preparation of necessary paperwork, sending the paperwork to the lender and following up with lenders regarding modification offers.

Therefore, had you established that your business satisfies the requirements of section 501(c)(3), and that you otherwise met the requirements of section 501(c)(3), your failure to satisfy the requirements of section 501(q) would prevent you from being exempt from taxation under section 501(a).

Failure to Establish Qualification for Recognition of Exempt Status

An applicant is required to submit sufficient information during the application process for the Service to conclude that the organization is in compliance with the organizational and operational requirements of section 501(c)(3) before a ruling is issued. Denial of exemption may be based solely upon failure to provide information describing in adequate detail how the operational test will be met. See La Verdad v. Commissioner and section 4.03 of Rev. Proc. 2012-9, above. In many instances, you did not provide explanations required by the application. For example, you did not explain how you applied for a HUD housing counseling agency even though your main source of income will be from HUD grants. In fact, you failed to provide a draft application form, which is the first step of being a HUD housing counseling agency. 40% of your activity consists of housing and financial seminars, workshops and classes. You did not show how you actually carry out such activities. Your reason for not having any plans or necessary draft form of applications is that you do not have any funds yet. Exemption from federal income tax is not a right but rather a matter of legislative grace. See New Dynamics Foundation, above. In addition, an organization has the burden of providing sufficient substantive information regarding its activities and operations to establish entitlement to tax-exempt status. See Harding Hospital, Inc. v. United States, above. Based on the facts presented, you failed to provide an adequate basis for us to determine that you are organized and operated exclusively for exempt purposes. See La Verdad v. Commissioner.

Conclusion

In summary, you are not operated exclusively for educational or charitable purposes. Specifically you fail the operational test for exemption under section 501(c)(3) of the Code because your housing counseling and resolution services are commercial in nature and you did

not establish that your net earnings will not inure in whole or in part to the benefit of private shareholders or individuals. You also fail to qualify under section 501(q) of the Code because your housing counseling and resolution services are not tailored to specific individuals' needs and you compensate all of your governing members. In addition, you failed to provide sufficient information in your application to enable us to determine that you are eligible for recognition of exempt status. Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns. Contributions to you are not deductible under section 170.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

Types of information that should be included in your appeal can be found on page 2 of Publication 892, under the heading "Regional Office Appeal". The statement of facts (item 4) must be accompanied by the following declaration:

"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

The declaration must be signed by an officer or trustee of the organization who has personal knowledge of the facts.

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to appeal as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in

part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to the applicable address:

Mail to:

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You may fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Holly O. Paz
Director, Exempt Organizations
Rulings and Agreements

Enclosure, Publication 892